

undertake actions necessary to ensure appropriately discounted rates for all specified entities.

The Commission will closely monitor how facilities-based competition develops throughout Kentucky. Accounting and monitoring measures will be developed in a workshop.

#### Workshops

All workshops, as discussed below, are to be formed as soon as possible. Workshop participants will have 90 days to make recommendations to the Commission for final decision. Each party should designate representatives for the USF workshops within 30 days of the date of this Order. Commission staff will schedule the first meeting as soon as possible.

Workshop participants should work in a spirit of compromise, attempting to resolve all relevant issues to implement the Commission's policies. Workshops will operate under the auspices of the Commission, and staff will have the authority to mediate when necessary. If staff mediation fails, i.e., no accord can be reached, the issue will be brought to the Commission for decision.

The following are specific issues to be addressed by the USF workshops:

#### A. Defining Rural and Urban Customers

The workshop shall work within the general guidelines set out above and shall formulate a definition of rural and urban areas which accomplishes the Commission's universal service goals, i.e., to encourage facilities-based competition in the rural as well

as urban parts of the state. The potential for distorted investment decisions which may occur as a result of subsidizing rural versus urban customers should be minimized.

For purposes of determining USF payments per household, there are many ways to define urban and rural areas. For example, the definition could be based on the number of access lines served by a central office. Using population density as a factor is also a possibility. For example, only those customers residing within a set number of miles from a central office serving more than 15,000 access lines might be considered "urban" customers.

However, effort must be made to minimize potential distortion of investment decisions resulting from USF funding policies. Distorted investment decisions may occur between neighboring exchanges belonging to different ILECs because of differing levels of USF support. USF payments are proposed to vary depending on each LEC's NTSRR. The workshop participants should attempt to formulate policies that will minimize such distortions while accomplishing universal service goals.

B. Appropriate Service Territory At Time Of Certification For Local Service

To some extent, the market will define the geographic boundaries that constitute any particular local calling area. It is also probable that ALEC-defined local calling areas may never precisely conform to current ILEC local calling areas. However, cherry picking should be avoided and all customers equitably served in a timely fashion. One possible solution is to require all ALECs to serve an entire urban area, however defined, through some combination of resale and their own facilities. This requirement would ensure that urban residential customers who do not have USF payments associated with

their households will be served in a timely fashion. To avoid preferential service offerings by ALECs, each ALEC should file as a special contract any off tariff rate pursuant to 807 KAR 5:011, Section 13, and should include appropriate cost support.

Situations in which USF payment unduly alters the investment decisions in ways that are contrary to the development of ubiquitous facilities-based competition should be avoided. Expansions of service territory outside an urban area may be defined by, at a minimum, end-office or exchange service territory. This definition would, at least, avoid service disparities within an exchange or area served by an end-office. For those ALECs planning to serve the entire state, such problems will not arise. Service territory issues will be covered in a workshop.

C. Monitoring Effectiveness Of Low-Income Programs

It is important to monitor the effectiveness of low-income programs and to address problems as they develop. The principal potential problem is, of course, failure to obtain acceptable increases in the state penetration rate. It may be appropriate to work with low-income support groups to isolate and track causes for such a problem. One obvious cause could be simple inability to pay the local portion of the telephone bill. Or perhaps the local portion of the bill is affordable, but not the toll portion. A standardized survey to be given to disconnecting, reconnecting, and new subscribers may help to pinpoint specific problems. In addition, a workshop, meeting on an as-needed basis, would provide a convenient forum for sharing data and discussing issues. Such a workshop could also coordinate surveys if necessary. The Commission will act as the organizing entity. Once new policies are implemented, penetration rate changes and other relevant

statistics such as reasons for disconnection, reconnection histories, and mitigating circumstances will be tracked for a three-year trial period. Also during this three-year period, the Commission will consider whether in-depth studies of Kentucky-specific universal service issues should be conducted. Established aid agencies may also be requested to assist in locating and working with households without telephones.

D. Fulfillment of Universal Service Goals and Diminution of the USF

Future workshop issues will be determining how and when universal service goals have been achieved and the means to reduce the USF to some minimum maintenance level. It is possible that in the presence of a fully competitive market, the USF will remain necessary to maintain basic local service affordability. The workshop may involve developing criteria to determine the competitive nature of the markets, including whether any one firm is able to exert undue influence.

E. Fund Administration

The Commission finds that USF administration costs should be rolled into ILECs' assessments. However, a second key decision, the selection of a USF administrator, remains to be determined perhaps through a workshop. There was no information in the record specifying pricing, a third key issue.

There are four options for a fund administrator regarding which parties may file comments within 30 days. The first option is a third party, such as National Exchange Carriers Association ("NECA"). The second option is BellSouth. Administration by BellSouth appears to be an extremely cost effective choice. The Commission would regularly monitor the fund and create an audit record of the fund under this option. The

third option is the Commission staff. Georgia has proposed this option and is issuing an order detailing the proposal. This option could also be extremely cost effective. The fourth option is to determine the fund administrator through a competitive bid process. The lower the cost of fund administration, the greater the benefit to Kentucky ratepayers.

#### RURAL COMPANY EXEMPTIONS

During the proceedings, the parties were asked if there were any economic arguments to support shielding rural telephone companies from competition. Generally, the parties responded that, although there are no economic reasons, there may be policy reasons. The ITG opined that the 1996 Act provides an exemption for small rural telephone companies in Section 251(f)(1).<sup>110</sup> The ITG further stated that the 1996 Act provides for a suspension of all 11 specific duties placed on ILECs in Section 251(f)(2).<sup>111</sup> Finally, the ITG asked the Commission to consider the pleadings, data responses, testimony and its brief as its petition for a suspension of all of the requirements imposed on ILECs in Sections 251(b) and (c) of the 1996 Act for a period of 10 years. TDS stated that the 1996 Act effectively provides small rural telephone companies an opportunity for gradual transition to local exchange competition and called for the Commission to grant the small, rural LECs a five-year suspension of competition pursuant to Section 251(f)(2) of the 1996 Act.<sup>112</sup>

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<sup>110</sup> ITG Brief at 4.

<sup>111</sup> Id.

<sup>112</sup> FCC Order at paragraph 1262.

Section 251(f)(1) of the 1996 Act grants rural telephone companies an exemption from Section 251(c) until the utility has received a bona fide request for interconnection and the state commission has determined that the request is not unduly economically burdensome, is technically feasible, and is consistent with universal service objectives. This exemption is applicable to each ITG company, ALLTEL, TDS, and part of GTE. Bona fide requests for interconnection have been received from AT&T and MCI in GTE's area and are pending Commission review.<sup>113</sup>

Section 251(f)(2) allows LECs with fewer than 2 percent of the nation's subscriber lines to petition a state commission for a suspension or modification of any requirements of Section 251(b) and (c). The FCC concluded that Congress intended Section 251(f)(2) only to apply to companies with fewer than 2 percent of subscriber lines nationwide at the holding company level.<sup>114</sup> Suspension or modification is granted if necessary to avoid a significant adverse economic impact on users of telecommunications services generally, to avoid imposing a requirement that is unduly economically burdensome or that is technically infeasible and is consistent with the public interest, convenience and necessity.<sup>115</sup> Suspension or modification may be requested by all Kentucky ILECs except BellSouth and GTE.

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<sup>113</sup> Case No. 96-313, Application of GTE South Incorporated for The Rural Telephone Company Exemption from Certain Requirements of the Telecommunications Act of 1996; and Case No. 96-440, Petition by MCI for Arbitration of Certain Terms and Conditions of a Proposed Agreement with GTE South Incorporated Concerning Interconnection and Resale under the Telecommunications Act of 1996.

<sup>114</sup> FCC Order at paragraph 1264.

<sup>115</sup> Id. at paragraph 1250.

The FCC has determined that the decision to allow a telephone company to maintain an exemption or to be granted a suspension or modification of Section 251 of the 1996 Act should be left to state commissions. Generally, the FCC opined that Congress intended exemptions, suspensions and modifications to be the exception and not the rule and to apply only to the extent and for the period of time that policy considerations justify such exemption, suspension or modification.<sup>116</sup> Congress did not intend to insulate smaller or rural telephone companies from competition.<sup>117</sup>

More specifically, the FCC stated that to justify a continued exemption under Section 251(f)(1) of the 1996 Act after receipt of a bona fide request, a LEC must offer evidence that application of those requirements would likely cause undue economic burdens beyond the economic burdens typically associated with efficient competitive entry. The FCC stated that those decisions should be made on a case-by-case basis.

It is clear from the FCC Order that under either Section 251(f)(1) or (2) of the 1996 Act, each utility asserting that an exemption should continue or claiming that a suspension or modification should be granted must prove that its specific claim is appropriate. Therefore, the ITG's request to have all of its members treated as a group is inconsistent with the 1996 Act and should be denied.

Whether a LEC seeks a suspension or modification under Section 251(f)(2) or the maintenance of an exemption under Section 251(f)(1), the Commission's inquiry will be substantially the same. These shields from competitive entry are temporary to allow

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<sup>116</sup> Id. at paragraph 1262.

<sup>117</sup> Id.

adequate time for preparation. The Commission expects rural ILECs to undertake all steps necessary to compete effectively in an expeditious manner.

Rural companies have generally not been required to do detailed cost studies. Accordingly, their pricing of interconnection and network elements will be a significant undertaking. Rate rebalancing, another action potentially necessary for competition, has not been fully addressed. Network modernization may be required by some rural companies. The cost study development, additional rate rebalancing, and network modernization may need to occur prior to effective competition in areas served by rural companies.

Any request to maintain an exemption or to be given a suspension or modification that relies on failure to complete the cost study, rate rebalancing, or network modernization must contain a specific schedule for addressing each of these items. As of three years from the date of this order, the Commission will no longer consider lack of compliance with these three items as an adequate basis in support of petitions to maintain an exemption or to be given a suspension or modification.

The Commission will fully and carefully review each petition balancing the company's need to prepare for competition and the potential benefits of competition. If a petition is approved, the Commission will attempt to maintain the exemption or grant the suspension or modification for a period it deems necessary for a company to prepare itself for competition. The Commission has been in the forefront nationally in encouraging interLATA and intraLATA toll competition and will continue to encourage competition in local exchange markets, balancing the interests of consumers and



telecommunications providers alike within the parameters mandated by Congress and the FCC.

### RATE REBALANCING

It is reasonable to expect competitive pressures to force ILECs to price local services closer to cost, requiring them to rebalance existing rates. Also, as competition increases, ILECs may seek to be regulated in some manner other than rate of return. The ITG has stated that its companies must be permitted to move toward price regulation and has proposed a simple price cap plan.<sup>118</sup> The ITG has also proposed to work out the details of its plan in a workshop. Most of the rural ILECs have not been before the Commission in a rate proceeding since the early 1980's. Given the significance of the change from rate of return to alternative regulation, it is critical to establish appropriate earnings at the outset of any new regulatory plan as was done for BellSouth prior to the adoption of its Price Cap Regulation Plan. Therefore, an ILEC wishing to rebalance its rates and to be subject to some form of regulation other than the regulatory scheme embodied in KRS Chapter 278 may be subject to a full earnings review. Alternative regulation and rate-rebalancing petitions will be considered on an individual company basis.

### MONITORING REQUIREMENTS

Competition in the local exchange market is unlikely to develop at the same pace throughout the state. As a result, it will be necessary for the Commission to evaluate

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<sup>118</sup> ITG Brief at 13.

whether the objectives of the 1996 Act relative to opening the local market are being achieved in all geographical areas of the state.

Therefore, the Commission will require each LEC to file the following information for Kentucky operations only: (1) Whether it is facilities-based or resale-based and the extent to which it is using its own facilities or is using unbundled elements or resold services obtained from an incumbent LEC; (2) Whether it plans to provide business and residential exchange and access service and the dates these services will be available. This information will be required only at the time of initial operations; (3) The number of access lines by type of customer served (business and residential); (4) A description of existing facilities; (5) A description of plans for future construction; (6) Traffic volumes by month for the six-month reporting period; (7) Areas served; and (8) Maps of service territory.

The information will be due by January 31 and July 31 of each year. The Commission will review the six-month filing requirement periodically and, if warranted, will change the reporting intervals.

In addition, ALECs will be required to file the "Report of Intrastate Gross Operating Receipts Report" for nondominant carriers pursuant to KRS 278.140. Those companies previously authorized to provide other telecommunications services should combine the intrastate revenues from those services with their local exchange and local exchange access revenues for reporting purposes.

### IMPLEMENTING LOCAL COMPETITION

The Commission favors a pro-competitive policy for all geographic areas of Kentucky and expects that the decisions made in this and subsequent orders will ensure compliance with the 1996 Act while providing the benefits of competition to all of the Commonwealth's citizens.

Accordingly, the Commission will allow implementation of local competition as soon as possible. Many negotiated interconnection agreements and arbitration petitions await Commission review, and will be dealt with as expeditiously as possible. In addition, the Commission finds it appropriate to alter its restrictions on CAPs. At present, CAPs doing business in Kentucky are authorized to provide access to IXCs' networks but prohibited from providing intraexchange traffic pending the establishment of a USF. This stricture is no longer in the public interest and is therefore abolished.

In addition, any authorized utility that has a final interconnection agreement or has necessary facilities in place, as well as an approved tariff for local service, may provide intraexchange local service under the following condition, pending establishment of a USF: it must demonstrate to the Commission that it has posted a bond or created an escrow account to pay its USF obligations in an amount equal to 6 percent of its gross receipts from the provision of intrastate service.<sup>119</sup> Refunds or additional payments

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<sup>119</sup> This percentage is based on the Commission's best estimate of universal service obligations of \$90 million and expected gross receipts during the first year following implementation of local competition of \$1.5 billion. The annual universal service obligation consists of NTSRR, Lifeline, and USF administrative costs.

may be required depending on the Commission's decisions regarding USF obligations after workshops have been held.

Carriers which have not yet been authorized to provide service in Kentucky and which plan to provide local service shall file a proposed tariff, and the following information: (1) the name and address of the company; (2) articles of incorporation or partnership agreement and certificate of authority to do business in Kentucky; (3) name, street address, telephone number and fax number (if any) of the responsible contact person for customer complaints and regulatory issues; (4) a notarized statement by an officer of the utility that the utility has not provided or collected for intrastate service in Kentucky prior to filing its application or, alternatively, a notarized statement by an officer that the utility has provided intrastate service and will refund all amounts so collected; (5) whether it plans to provide business and residential exchange and access service and the dates these services will be available; and (6) whether it will be facilities-based or resale-based and the extent to which it will use its own facilities or unbundled elements or resold services of an ILEC. Carriers planning to construct facilities to provide local exchange service shall, of course, comply with KRS 278.020.

Further, the Commission finds that all carriers providing local service should fully comply with Commission statutes and regulations unless specific exemptions are granted pursuant to KRS 278.512. In addition, all carriers providing local service shall obtain, and shall retain for one year, electronic or written evidence that each of its customers knowingly chose it as his local exchange carrier.

The Commission, having considered the extensive record, and being otherwise sufficiently advised, HEREBY ORDERS that:

1. Commission approved, negotiated arrangements for interconnection shall be the primary means for implementing local competition and, thus, Kentucky-specific rules shall not be implemented.

2. Interconnection and unbundling workshops shall not occur at this time.

3. No minimum list of services subject to resale will be established at this time.

4. On an interim basis, a single discount rate of 19.20 percent is established for BellSouth; a single discount rate of 18.81 percent is established for GTE; and a single discount rate of 17 percent is established for all other ILECs.

5. Avoided cost studies as prescribed herein shall be filed as soon as available, but unless otherwise ordered by the Commission, not later than 12 months from the date of this Order. Exempted utilities shall file avoided cost studies, unless otherwise ordered by the Commission, not later than 3 years from the date of this Order.

6. Workshops shall be conducted on all issues related to universal service and the USF.

7. Within 30 days of the date of this Order, parties may file comments to be considered in the universal service workshops.

8. Per the 1996 Act, the ITG companies, ALLTEL, and the TDS companies are exempted until and unless a bona fide request for interconnection is received and the Commission addresses the public interest issues; however, the ITG request for a

blanket exemption for a set number of years is denied. But, the Commission shall review requests for suspensions and modifications on a company-specific basis.

9. After three years of the date of this Order, the Commission shall not consider failure to complete a cost study, rate rebalancing or network modernization to enable competition as an adequate basis for maintaining an exemption or granting a suspension or modification.

10. Petitions for rate rebalancing shall be considered on a company-specific basis.

11. All LECs shall comply with the monitoring requirements set forth herein.

12. An authorized utility may provide local service immediately upon complying with the following conditions:

- a. An approved interconnection agreement or facilities.
- b. An approved local service tariff.
- c. A bond posted or an escrow account to pay its USF obligations in an amount equal to 6 percent of its gross receipts from the provision of intrastate service.

13. CAPs previously authorized to serve shall no longer be restricted from providing intraexchange traffic.

14. Any carrier not yet authorized to provide service in Kentucky and which plans to provide local service shall include in its application a proposed tariff and each of the items specified herein.

15. All carriers providing local service shall fully comply with Commission statutes and regulations unless specific exemptions are granted pursuant to KRS 278.512.

Done at Frankfort, Kentucky, this 26th day of September, 1996.

By the Commission

ATTEST:

  
Executive Director